HY'S OF CANADA LTD.

hy's

Bankers

Bank of Nova Scotia

Transfer Agents

Canada Permanent Trust
Toronto and Vancouver.

Stock

Listed on the Toronto and
Vancouver Exchanges.

Directors of the Company

Hy Aisenstat	President, Hy's of Canada Ltd.
Don Rosebourne	Vice President, Hy's of Canada Ltd.
Bernie Aisenstat	Vice President, Operations, Hy's of Canada Ltd.
Joe Garfin	Real Estate Manager, Hy's of Canada Ltd.
Jack Shatz	Eastern Division Manager, Hy's of Canada Ltd.
Alan Eyre	President, Dueck on Broadway Ltd.
Arthur R. Smith	President, International Jet Air Ltd.
Richard C. Baxter	Chairman, The Baxter Group Ltd.

Directors' Report to Members

Included in this report are financial statements, with accompanying notes and Auditors' Report, which set out details of the Company's financial activities for the year ended September 30, 1976.

Despite an increase in revenue from $14,062,000 to $15,735,000, net earnings declined from 51¢ per share in 1975 to 12¢ per share in 1976. A significant portion of this can be attributed to the higher depreciation and amortization expenses which rose some $240,000 during the current period. Added to this is the substantially higher interest expense on borrowings.

Your Company undertook a major expansion and refurbishing programme during the year in excess of $3,000,000 and the fruits of this have yet to be realized. Alongside the expansion we were faced with a very difficult year in terms of the lesser than anticipated tourist traffic, and this was particularly evident in British Columbia where we have a high concentration of operations. Results from our hotel affiliate in the Okanagan contributed significantly to the lower earnings as a result of the extremely poor summer experienced there.

In our report last year we expected that 1976 would be a transitional year for the Company but were unable to predict the lower earnings actually suffered. On the brighter side we are pleased to announce that subsequent to the fiscal year end we have opened our new Hy's Steak House in Honolulu to excellent acceptance from both the critics and the public and this restaurant will undoubtedly have a meaningful affect upon our 1977 earnings. Your Company had over 900 employees at September 30, 1976 with an annual payroll of $4,950,000 compared to $3,900,000 the previous year.

In view of the current uncertain economic conditions we have curtailed any expansion for the time being, despite the fact that we have investments in several projects. It is expected and hoped that 1977 will indicate and confirm your Directors' faith in the Company with both increased sales and profit. As a reflection of this the Company continued in 1976 to purchase its shares on the open market.

On Behalf of the Board

President

Consolidated Balance Sheet

September 30, 1976

Assets

	1976	1975
Current		
Cash	$ 374,000	$ 225,000
Accounts receivable (note 2)	527,000	776,000
Inventories, at cost which is lower than net realizable value	564,000	560,000
Prepaid expenses and deposits	195,000	157,000
Due from directors and officers	11,000	12,000
	1,671,000	1,730,000
Investments		
Affiliated companies (note 1(b))	352,000	273,000
Other, at cost (note 3)	220,000	194,000
	572,000	467,000
Fixed, at cost		
Buildings and leasehold improvements	7,942,000	6,020,000
Furniture and equipment	2,719,000	2,110,000
	10,661,000	8,130,000
Less: Accumulated depreciation	3,246,000	2,468,000
	7,415,000	5,662,000
Land	1,277,000	516,000
	8,692,000	6,178,000
Other		
Deferred development expenses, contract rights and other intangibles, less amortization of $584,000 (1975 — $724,000)	451,000	487,000
	$ 11,386,000	$ 8,862,000

Approved on behalf of the Board:

DIRECTOR

DIRECTOR

Liabilities

	1976	1975
Current		
Bank indebtedness (note 4)	$ 596,000	$ -
Accounts payable and accrued expenses	1,536,000	1,316,000
Income taxes payable	237,000	264,000
Current portion of long term debt (note 5)	588,000	129,000
Deferred income taxes	91,000	62,000
	3,048,000	1,771,000
Long term debt, less current portion shown above (note 5)	3,927,000	2,637,000
Deferred income taxes	313,000	371,000
Minority interest	163,000	127,000
	7,451,000	4,906,000

Shareholders' Equity

	1976	1975
Share capital (note 6)	2,071,000	2,071,000
Retained earnings	1,946,000	1,941,000
	4,017,000	4,012,000
Less: Treasury shares (note 6(c))	82,000	56,000
	3,935,000	3,956,000

Commitments and contingent liabilities [**note 10**]

	1976	1975
	$11,386,000	$ 8,862,000

The accompanying notes are an integral part of this financial statement.

Consolidated Statement of Earnings

For the Year Ended September 30, 1976

	1976	1975
Income		
Sales	$15,465,000	$13,635,000
Management and rental income	294,000	259,000
Share of earnings (loss) of affiliates	(24,000)	168,000
	15,735,000	14,062,000
Expenses		
Cost of sales and administration	13,322,000	11,596,000
Interest (note 5(c))	414,000	227,000
Real estate expenses and rent	885,000	814,000
Depreciation	692,000	500,000
Amortization of deferred development expenses, contract rights and other intangibles	211,000	160,000
	15,524,000	13,297,000
Earnings before undernoted items	211,000	765,000
Provision for income taxes		
Current	222,000	240,000
Deferred	(42,000)	114,000
	180,000	354,000
	31,000	411,000
Minority interest in net losses of subsidiaries	69,000	24,000
Earnings before extraordinary items	100,000	435,000
Extraordinary items (note 7)	6,000	39,000
Net earnings for the year	$ 106,000	$ 474,000
Earnings per share		
Earnings before extraordinary items	12¢	51¢
Net earnings for the year	12¢	55¢

The accompanying notes are an integral part of this financial statement.

Consolidated Statement of Retained Earnings

For the Year Ended September 30, 1976

	1976	1975
Retained earnings, beginning of the year	$1,941,000	$1,688,000
Less: Dividends (note 8)	86,000	171,000
Part IX taxes (note 8)	15,000	27,000
Income taxes deferred in prior years	-	23,000
	101,000	221,000
	1,840,000	1,467,000
Add: Net earnings for the year	106,000	474,000
Retained earnings, end of the year	$1,946,000	$1,941,000

The accompanying notes are an integral part of this financial statement.

Consolidated Statement of Changes in Financial Position

For the Year Ended September 30, 1976

	1976	1975
Source of working capital		
Operations —		
Earnings before extraordinary items	$ 100,000	$ 435,000
Amounts not requiring a current outlay of funds		
Amortization	211,000	160,000
Depreciation	692,000	500,000
Deferred income taxes (non-current portion)	(58,000)	104,000
Minority interest	(69,000)	(24,000)
Undistributed (earnings) loss of affiliates	24,000	(62,000)
	900,000	1,113,000
Long term borrowing	1,619,000	1,678,000
Construction accounts payable	275,000	-
Proceeds from sale of fixed assets and shares of subsidiary	-	292,000
Investment by minority interest	50,000	(32,000)
Reduction in investments in affiliates	170,000	(18,000)
	3,014,000	3,033,000
Application of working capital		
Repayment of long term debt	145,000	301,000
Increase (decrease) in current portion of long term debt	459,000	(91,000)
	604,000	210,000
Fixed asset additions	3,056,000	2,265,000
Other investments, net	20,000	9,000
Deferred development expenses and other intangibles	125,000	138,000
Purchase of treasury shares	26,000	42,000
Dividends	86,000	171,000
Part IX taxes	15,000	27,000
Income taxes deferred in prior years	-	23,000
Increase in investments in affiliates	313,000	-
Investment in non-current assets of subsidiary	105,000	-
	4,350,000	2,885,000
Decrease [increase] in working capital deficiency	(1,336,000)	148,000
Working capital [deficiency], beginning of the year	(41,000)	(189,000)
Working capital [deficiency], end of the year	$(1,377,000)	$ (41,000)

The accompanying notes are an integral part of this financial statement.

Notes to the Consolidated Financial Statements

September 30, 1976

1. Significant accounting policies

(a) Basis of consolidation — The consolidated financial statements include the accounts of Hy's of Canada Ltd. and all of its subsidiaries:

B & B Management Ltd.
Babs Management Ltd.
Bernbourne Management Ltd.
Boyd Investments Ltd.
Carman Investments Ltd.
Duke Management Ltd.
Enrose Management Ltd.
Hycate Holdings Ltd.
Hydon Holdings Ltd.
Hy's of Chicago Ltd., and its subsidiaries Hy's of Hawaii, Ltd. (80% owned) and Kobe Japanese Steak House (Hawaii) Ltd. (70% owned)
Hy's Steak House (Eastern) Limited
Jet-Line Services Ltd., and its wholly-owned subsidiary, Hy's Steak House Ltd.
The Steak Loft Ltd.
Twelve Caesars Restaurant Ltd. (51% owned)

The accounts of Kobe Japanese Steak House (Hawaii) Ltd. have been consolidated from the date of acquisition, June 2, 1976. Hy's of Hawaii, Ltd. was incorporated during the year and commenced restaurant operations subsequent to September 30, 1976.

(b) Investments — Investments in 50% owned affiliated companies are accounted for by the equity method. Investments in other affiliates (less than 50% owned) are accounted for by the cost method.

The consolidated balance sheet item "Investments — Affiliated companies" is comprised of:

	1976	1975
Advances	$122,000	$128,000
Shares, at cost	321,000	51,000
Equity in earnings (net) of 50% owned affiliates, less dividends received since acquisition of shares	(91,000)	94,000
	$352,000	$273,000

On December 31, 1975, the Company increased its ownership in the Village Green Hotel companies to 50%. The cost of investments in these affiliates exceeded the Company's share of net asset values by $493,000 as of December 31, 1975. This excess is being amortized on the basis described in note 1(f) below.

The Company's investment in Kobe Japanese Steak House Ltd. was sold during the year for $120,000.

Notes to the Consolidated Financial Statements

September 30, 1976

1. **Significant accounting policies** (continued)

   (c) Foreign exchange — Assets, liabilities, income and expenses of operations in the United States have been converted to Canadian dollars at par . Use of average and year end exchange rates would not result in any material adjustment.

   (d) Joint venture — The consolidated financial statements include the Company's proportionate share of the assets, liabilities, income and expenses of an unincorporated joint venture. The Company is contingently liable for the total obligations of the joint venture. However, the total assets of the venture are available to satisfy such obligations.

   (e) Depreciation — The provision for depreciation is calculated by the straight line method for all assets except automotive equipment which is calculated by the declining balance method. The estimated useful life of the assets concerned is six years for automotive equipment, forty years for buildings, not more than ten years for furniture and equipment, and not more than the term of the lease plus the first renewal for leasehold improvements.

   (f) Deferred development expenses, contract rights and other intangibles:

      i. The companies capitalize as deferred development expenses all expenses incurred for a new restaurant prior to opening, plus any operating loss for the first three months of operations (before depreciation and amortization). These costs are then amortized over a three year period.

      ii. Contract rights are amortized over the terms of the agreements.

      iii. Other intangibles, including share issue expenses, goodwill and excess of cost of shares over net asset values of subsidiaries and 50% owned affiliates are amortized over twenty years.

   (g) Rounding — All dollar amounts are presented to the nearest $1,000.

2. **Accounts receivable**

   Accounts receivable in 1975 included $180,000 which was due on the sale of a subsidiary. The amount was received in the current year.

3. **Other investments**

   This category includes marketable securities, an interest in a restaurant partnership and miscellaneous investments. The carrying value of marketable securities ($165,000) is not significantly below quoted market prices. However, as a substantial number of shares the Company owns in a public restaurant company are subject to a pooling agreement, the quoted market price may not be indicative of the value of these shares.

4. **Bank indebtedness**

   Current bank indebtedness includes subsidiaries' loans of $480,000 which are guaranteed by the Company. Security for the Company's bank indebtedness is described in 5(a).

PLAZA II

5. Long term debt

	1976		1975	
	Amount	Due within one year	Amount	Due within one year
Bank term loan — bank prime rate plus 1-½%, see (a) below	$2,550,000	$443,000	$1,575,000	$ -
Construction loan and accounts payable, see (b) below	375,000	68,000	-	-
Mortgages payable — 9% to 12% maturing from 1978 to 1983	1,553,000	40,000	1,042,000	30,000
Other	37,000	37,000	149,000	99,000
	$4,515,000	$588,000	$2,766,000	$129,000

(a) i. A supplemental loan agreement authorized by the Company's bankers prior to September 30, 1976 was executed by the Company subsequent to the year end. The agreement provides for a non-revolving term loan and an operating loan. Security for the loans, provided by the Company and certain subsidiaries, includes (1) general assignments of book debts, (2) pledge of marketable securities, (3) specific charges on certain fixed assets and (4) a floating charge upon all real and personal property subject to specific prior encumbrances. The debenture issued to the bank contains covenants which require, among other things, (1) the maintenance of a defined working capital ratio and (2) bank approval of capital expenditures.

The term loan is payable on demand, but the bank has agreed, except in the event of default, to allow repayment in consecutive monthly blended installments from October 1976 to August 1981.

ii. At September 30, 1976 the companies were in default of the debenture covenant relating to their working capital ratio. The default has continued since the year end. The bank has agreed to waive the default on the understanding that the companies will comply with the covenant by not later than June 30, 1977.

(b) At September 30, 1976 the Company had received $100,000 (U.S.) of an authorized $425,000 (U.S.) term bank loan for use in financing restaurant construction by a subsidiary. Security for this loan includes the items described in (a) above and, in addition, a second mortgage on the particular restaurant facility. The loan, which bears interest at United States bank rates plus 1-½%, is repayable over a five year term. Subsequent to the year end a subsidiary negotiated a loan in the United States to replace the loan incurred by the Company.

Notes to the Consolidated Financial Statements

September 30, 1976

5. **Long term debt** (continued)

   Construction accounts payable of $275,000 have been classified as long term debt, representing the unadvanced portion of the construction loan ($325,000) less estimated construction costs for this facility incurred subsequent to the year end of $50,000.

   (c) Interest incurred during the year on long term debt amounted to $342,000 (1975 — $214,000).

6. **Share capital**

   (a)Authorized

   1,000,000 shares, no par value

   (b) Issued

870,000 shares	$2,071,000

(c) Treasury shares	**Balance September 30, 1975**	**Acquired during the year**	**Balance September 30, 1976**
Number of shares	17,000	9,000	26,000
Cost	$56,000	$26,000	$82,000

The quoted market price of these shares at September 30, 1976 was $62,000 (1975 — $50,000).

7. **Extraordinary items**

   The amount shown on the consolidated statement of earnings as "extraordinary items" is net of deferred income taxes of $2,000 (1975 — $19,000) and is comprised of:

	1976	**1975**
Gain on sale of shares in subsidiary	$ -	$59,000
Gain (loss) on sale of other assets	6,000	(15,000)
Reduction in carrying value of advances to an affiliate and miscellaneous investments	-	(5,000)
	$6,000	$39,000

Notes to the Consolidated Financial Statements

September 30, 1976

HY'S of Yorkville

8. Dividends

During the year the Company increased its tax-paid undistributed surplus on hand by the payment of taxes of $15,000 (1975 — $27,000). Dividends paid out of tax-paid undistributed surplus during the year amounted to $86,000 (1975 —$171,000).

9. Remuneration of directors and senior officers

	1976	1975
Eight directors in their capacity of directors	$ 18,000	$ 20,000
Five senior officers	225,000	203,000
	$243,000	$223,000

10. Commitments and contingent liabilities

(a) Lease rentals — Minimum rentals, excluding rentals based on a percentage of sales, under existing lease agreements will be approximately $503,000 annually over the next five years. Total rent incurred for the year ended September 30, 1976 including rent based on a percentage of sales amounted to $702,000 (1975 — $625,000).

(b) Projects in progress — The estimated costs to complete construction in progress at September 30, 1976 are approximately $100,000.

(c) Guarantees — The Company is contingently liable as guarantor of loans and advances to affiliated companies and others up to $1,808,000. Other parties have indemnified the Company in the amount of $687,000.

11. Anti-Inflation legislation

The companies are subject to the Anti-Inflation Act and Regulations. In the opinion of management, the companies have no material unrecorded liabilities or contingent liabilities in respect thereof.

Auditors' Report

To the Shareholders of
Hy's of Canada Ltd.

We have examined the consolidated balance sheet of Hy's of Canada Ltd. and subsidiary companies as at September 30, 1976 and the consolidated statements of earnings, retained earnings and changes in financial position for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the companies as at September 30, 1976, and the results of their operations and the changes in their financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Collins Barrow

Chartered Accountants

Vancouver, Canada
January 18, 1977 (except for note 5(a) ii
as to which the date is March 3, 1977).

Hy's Steak House,
73 Richmond Street West,
Toronto, Ontario

Hy's Yorkville,
133 Yorkville Avenue,
Toronto, Ontario

Hy's Steak Loft,
216 Kennedy Street,
Winnipeg, Manitoba

Hy's Steak House,
Midtown Plaza,
Saskatoon, Sask.

Hy's,
316 - 4th Avenue S.W.,
Calgary, Alberta

Hy's Encore,
637 Hornby Street,
Vancouver, B.C.

Hy's at the Sands,
1755 Davie Street,
Vancouver, B.C.

Hy's Prime Rib,
1177 West Hastings Street,
Vancouver, B.C.

Plaza II,
1075 West Georgia Street,
Vancouver, B.C.

12 Caesars Restaurant,
595 Hornby Street,
Vancouver, B.C.

Hy's Steak House
777 Douglas Street,
Victoria, B.C.

Hy's,
100E Walton,
Chicago, Illinois

Hillside Inn,
Hillside Shopping Centre,
3102 Shelbourne Street,
Victoria, B.C.

Hy's,
Honolulu, Hawaii

Kobe Japanese Steak House,
Honolulu, Hawaii

Village Green Inn,
141 Trans Canada Highway,
Duncan, B.C. (Affiliate)

Village Green Inn,
Vernon, B.C. (Affiliate)

Sherlocks on Sheppard,
Toronto, Ontario

Bartholomews,
777 Douglas Street,
Victoria, B.C. (Affiliate)

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